

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF IOWA
EASTERN DIVISION

UNITED STATES OF AMERICA,)	No. CR 12-2021 LRR
)	
Plaintiff,)	GOVERNMENT'S SENTENCING
)	MEMORANDUM
vs.)	
)	
RUSSELL R. WASENDORF, SR.,)	
)	
Defendant.)	

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Pursuant to the Court's Order Setting Sentencing Hearing, the government submits the following memorandum to address issues to be decided by the Court at sentencing. The sentencing hearing is currently scheduled for January 31, 2013, at 9:00 a.m.

I. SUMMARY OF THE CASE

- A. Witnesses: FBI SA Scott Irwin
Shannon Marsh
Brenda Cuypers
- B. Exhibits: Exhibit 1: 7/9/12 Windjammer Filing
Exhibit 2: 7/9/12 FRX Daily Segregation Report with backup
Exhibit 3: 7/9/12 FRX Daily Segregation Report (revised)
Exhibit 4: Fake US Bank Statement - May 2012
Exhibit 5: Real US Bank Statement - May 2012
Exhibit 6: Real US Bank Statement - June 2012
Exhibit 7: Real US Bank Statement - July 2012
Exhibit 8: 7/6/12 Daily Equity Report
Exhibit 9: Irwin Loss Summary
Exhibit 10: Victim List
- C. Issues:
- (1) Whether a 28-level enhancement should apply pursuant to USSG §2B1.1(b)(1)(O) based upon a loss exceeding \$200,000,000 (see PSR ¶¶ 43, 44 at 51);
 - (2) Whether a two-level enhancement should apply pursuant to USSG §2B1.1(b)(10)(C) for sophisticated means (see PSR ¶ 52); and
 - (3) The amount of restitution and manner of distribution (see PSR ¶¶ 117, 118 and 119).

II. THE ACTUAL LOSS EXCEEDS \$200,000,000

Defendant objects to the scoring of a 28-level enhancement under USSG §2B1.1(b)(1)(O) based upon a loss exceeding \$200,000,000. (See PSR ¶¶ 43, 44 at 51). In conclusory fashion, defendant claims the loss is less than \$200,000,000. (PSR

Addendum (Defendant's Objections 5 and 7)).¹ Defendant's objection should be overruled. As calculated in the PSR, the loss in this case exceeds \$215,000,000. (See PSR ¶¶ 43-44; Gov. Ex. 9).

A. Legal Standards

The burden is on the government to prove by the preponderance of the evidence the amount of loss. See *United States v. Staples*, 410 F.3d 484, 490 (8th Cir. 2005).

Loss is the greater of either actual loss or intended loss. USSG §2B1.1, comment (n.3(A)). Actual loss "means the reasonably foreseeable pecuniary harm that resulted from the offense." USSG §2B1.1, comment (n.3(A)(i)). "The court only needs to make a reasonable estimate of the loss." USSG §2B1.1, comment (n.3(c)). See also *United States v. Waldner*, 580 F.3d 699, 705 (8th Cir. 2009) ("Because the loss caused by fraud is often difficult to determine precisely, 'a district court is charged only with making a reasonable estimate of the loss.'" (citation omitted)).

While the loss in some fraud cases can be difficult to determine, the actual loss in this case can be calculated with remarkable precision. As of the start of business on July 9, 2012, PFG's customers had deposited approximately \$376,999,120.99² with

¹ In their plea agreement, the parties stipulated an upward adjustment of at least 26 levels applies under USSG §2B1.1(b)(1)(N) based upon a loss in excess of \$100,000,000. (PSR ¶ 3).

² Depending upon the time of day on July 9, 2012, that a calculation is performed, these figures change to a relatively insignificant degree. For example, the amount of customer funds required to be segregated was \$376,999,120.99 when calculated by Shannon Marsh at the start of the day on Monday, July 9, 2012, using figures for the close of business on July 6, 2012. (See Gov. Ex. 1-2, 9). When the calculation was revised by CFO Brenda Cuypers later on July 9, 2012 (after defendant's fraud was revealed), the amount had changed to \$376,997,999.38 due to the day's account activity. (See Gov. Ex. 3). Generally, while the presentence report uses the revised figures from later in the day on July 9, 2012, FBI Special Agent Irwin's loss summary (Gov. Ex. 9) uses the figures as of the close of business on July 6, 2012 (reflecting the figures reported to the NFA on the morning of July 9, 2012 - see Gov. Ex. 1).

PFG that was supposed to be held in segregated accounts. (Gov. Ex. 1-2, 9). That same day, PFG's general ledger showed it had \$382,223,056.38 in segregated funds, resulting in \$5,223,935.39 in purported "Excess Seg Funds." (Gov. Ex. 1-2, 9). However, of the \$382,223,056.38 in supposedly segregated funds, \$220,754,483 of it did not actually exist. That is, while defendant's fabricated bank records caused PFG's general ledger to show the US Bank customer segregated account contained \$225,868,593.28 (Gov. Ex. 2, 8), in fact, the account contained \$5,114,110 (Gov. Ex. 7, 9). When shortfall in the US Bank customer segregated account (\$220,754,483) is subtracted from the amount purportedly in segregation on the morning of July 9, 2012, the amount actually in segregation becomes \$161,468,574. (Gov. Ex. 9). The result is that, as of the morning of July 9, 2012, a total of **\$215,530,547** of the funds required to be segregated was missing.³

The government respectfully asks that defendant's objection to PSR paragraphs 43, 44 and 51 be overruled.

III. THE OFFENSE INVOLVED SOPHISTICATED MEANS

Defendant objects to an enhancement for sophisticated means under USSG §2B1.1(b)(10)(C), claiming very basic, simple means were used to execute his fraud. (PSR ¶ 52). While some of defendant's individual acts might be characterized as simple in isolation, they were part of an exceedingly complex scheme whereby defendant's entire business was used as a mechanism to gather and purloin investor funds.

³ The same result is achieved by taking the \$220,754,483 shortfall in the US Bank customer segregated account, and crediting back the \$5,223,935.39 in purported "Excess Seg Funds."

A. Legal Standards

A sentence should be enhanced by two levels if “the offense otherwise involved sophisticated means.” USSG §2B1.1(b)(10)(C). The government must show that the offense involved “especially complex or especially intricate offense conduct pertaining to the execution or concealment of an offense.” *Id.*, comment (n.8(B)). In other words, the government must show defendant’s conduct was “notably more intricate than the garden variety” fraud. *United States v. Hance*, 501 F.3d 900, 909 (8th Cir. 2007) (“the government must show that Hance’s mail fraud, when viewed as a whole, was notably more intricate than that of the garden-variety mail fraud scheme”). “Repetitive and coordinated conduct, though no one step is particularly complicated, can be a sophisticated scheme.” *United States v. Finck*, 407 F.3d 908, 915 (8th Cir. 2005).

B. Argument

Here, defendant’s fraudulent scheme was far more sophisticated than the typical fraud. Indeed, at least since the early 1990s, defendant operated PFG as little more than a complex mechanism to fraudulently obtain and misuse investor’s funds. On this basis alone, a sophisticated means enhancement should apply.

As noted in the uncontested portions of the presentence report, PFG’s Futures Commission Merchant (FCM) registration was originally financed by J.C. in 1992. Shortly afterward, in 1993 or 1994, J.C. wanted to pull out his money, and defendant lacked the capital to keep PFG in business. (PSR ¶ 37). Defendant stole the required capital – at least \$250,000 – from PFG’s customer segregated funds, and used the money to buy out J.C. (PSR ¶ 37). Using a copy machine (see PSR ¶ 16), defendant fabricated a bank statement to conceal the theft of funds. (PSR ¶ 37). From that point forward, as defendant well knew, PFG was never profitable. (PSR ¶¶ 37-38). Rather, it

incurred tens of millions in losses over the next approximately 20 years. (PSR ¶ 38). Fueled by misappropriated investor funds, defendant fraudulently “grew” PFG so as to create the appearance it was a legitimate and successful FCM. This was a fundamental component of defendant’s scheme. As recounted in the presentence report, defendant stated he believed “if he could make himself appear rich, the auditors and regulators wouldn’t be concerned with the state of his personal finances and not discover it was all a fraud.” (PSR ¶ 38). By July 9, 2012, investors unwittingly entrusted more than \$376,000,000 to defendant and his fraudulent business. (Gov. Ex. 1, p. 4). Thus, defendant’s operation of PFG was, itself, “especially complex or especially intricate offense conduct pertaining to the execution . . . of [his] offense[s].” USSG §2B1.1, comment (n.8(B)).

Moreover, in order for the fraud to be effective and sustainable for years, defendant routinely created and used false certifications and forged documents to deceive his customers, his accounting department, his fellow corporate officers, an outside auditor, and multiple regulatory agencies whose core function was to detect and prevent exactly the type of criminal activity defendant perpetrated. The following are some of the sophisticated steps defendant took in order to execute and conceal his fraud over the years:

- In order to be able to steal the money without anyone knowing it, defendant used “blunt authority” to establish rules and procedures at PFG so that he was the only one to examine actual US Bank statements. (PSR ¶ 28).
- Defendant stole money by personally executing transfers from the US Bank account and then using photocopy and computer technology to forge bank statements that excluded the transfers and inflated the balance accordingly. (PSR ¶¶ 16-17).
- Defendant also stole money by fabricating large deposits into the US Bank account and then forging bank paperwork to substantiate the purported deposits

and, ultimately, inflate the balance. The fabricated deposits caused PFG's books to show "excess seg" where none actually existed. PFG's accounting department would then transfer the purported "excess seg" over to PFG's house account to be used for routine business purposes and capitalization requirements. The forged paperwork required for just this aspect of the scheme included deposit slips, copies of bank checks, and bank statements. (PSR ¶ 17). These documents, in turn, caused PFG's general ledger and subsidiary financial records and reports to be manipulated – all so that defendant could steal additional customer funds. (See PSR ¶ 17; Gov. Ex. 2 (7/9/12 FRX Daily Segregation Report with backup)).

- To conceal his fraud from regulators, defendant caused falsified daily segregation reports to be electronically submitted to the CFTC and NFA. (PSR ¶¶ 18 and 33; see Gov. Ex. 1 (7/9/12 Windjammer Filing)).⁴
- Also to conceal his fraud from regulators, defendant caused falsified monthly segregation reports (CFTC FORM 1-FR-FCM) to be sent to the CFTC. (See PSR ¶ 19).
- Also to conceal his fraud from regulators, defendant caused PFG's Chief Financial Officer to send falsified year-end financial statements – including inflated customer segregation totals – to be sent to the CFTC. (PSR ¶ 32).
- In order to conceal his crimes from the NFA's auditors, defendant intercepted account verification forms for the U.S. Bank account and forged purported responses from U.S. Bank. (PSR ¶ 20). This aspect of the scheme required defendant to establish a Cedar Falls post office box (P.O. Box 706) under his control and then cause auditors to send verification paperwork to the post office box. Defendant falsely certified the account balances under the forged signature of a US Bank representative. (See PSR ¶ 35). In order to make auditors believe P.O. Box 706 belonged to US Bank, defendant consistently changed US Bank's mailing address to "P.O. Box 706" on forged bank statements. (PSR ¶¶ 20, 28; Gov. Ex. 4).
- During an NFA audit in 2011, defendant's crimes were nearly discovered when two PFG employees (other than defendant) became involved in the account verification process. In order to prevent the discovery of the actual account balance by PFG personnel and the NFA, defendant flew from Chicago to Iowa, convinced a PFG employee that a clerk had pulled the wrong balance for the

⁴ The United States Commodity Futures Trading Commission (CFTC) is an independent federal regulatory agency responsible for administering and enforcing the provisions of the Commodity Exchange Act, 7 U.S.C. §§ 1 et seq. (2006), as amended, and the Regulations promulgated thereunder, 17 C.F.R. §§ 1.1 et seq. (2012). The National Futures Association (NFA) is a not-for-profit industry membership corporation (and registered futures association authorized under 7 U.S.C. § 21) that is responsible, under CFTC oversight, for certain aspects of the regulation of futures entities. (PSR ¶¶ 8-9).

account, convinced US Bank personnel that the confirmation form they had received had the wrong address on it, obtained a copy of the confirmation form, altered the confirmation form to reflect the inflated balance, altered his home fax machine to print "US Bank, Cedar Falls, IA" in the fax header, and then used his home fax machine to fax the fabricated form to the NFA. (PSR ¶ 39).

- Defendant similarly manipulated account verification procedures employed by PFG's auditor. (PSR ¶ 20).

These steps constituted sophisticated means to both execute and conceal defendant's offense.

In *United States v. Halloran*, 415 F.3d 940, 945 (8th Cir. 2005), the Eighth Circuit Court of Appeals affirmed the sentencing court's application of a sophisticated means enhancement in a case involving a far less complex scheme.

To accomplish his multi-layered plot, Halloran required the use of a corporate entity, numerous fraudulent documents and forged notary stamps. His elaborate scheme also required him to manipulate official property records by recording fictitious transfers of property and to exploit numerous individuals by forging their signatures on various fraudulent documents.

Id. at 945. The offense conduct in this case was far more sophisticated. Defendant used a corporate entity (PFG) and its subsidiaries as a mechanism to gather investors – and then steal their money – over the course of nearly two decades. Defendant forged an array of documents – including bank records and account verification forms. He manipulated PFG's general ledger by recording fictitious deposits into the US Bank account (in addition to hiding regular transfers from the account). He also forged the signatures of US Bank officials as part of his efforts to deceive regulators. Indeed, defendant's scheme would not have been possible without defendant's elaborate and sophisticated efforts to deceive regulators in this highly-regulated part of the financial services industry. These included defendant's use of P.O. Box 706 and his falsification of scores of legally-required regulatory reports.

Defendant's objection to the scoring of a two-level enhancement for sophisticated means, pursuant to USSG §2B1.1(b)(10)(C), should be overruled.

IV. GUIDELINES CALCULATION AND SENTENCE

In accordance with paragraphs 48 through 62 of the presentence report, the Court should calculate defendant's Total Offense Level as follows:

Base Offense Level: Pursuant to USSG §2B1.1(a), defendant's base offense level is 7.

Amount of Loss: An upward adjustment of 28-levels is appropriate under USSG §2B1.1(b)(1)(O) based upon an amount of loss in excess of \$200,000,000.

Sophisticated Means: A two-level upward adjustment is appropriate under USSG §2B1.1(b)(10)(C) based upon the offense involving sophisticated means.

Commodities Law Violation / Officer of a Futures Commission Merchant: A four-level upward adjustment is appropriate under USSG §2B1.1(b)(18)(B) because the offense involved a violation of commodities law and defendant was an officer and director of a futures commission merchant.

Number of Victims: A six-level upward adjustment is appropriate under USSG §2B1.1(b)(2)(C) based upon the offense involving more than 250 victims.

Acceptance of Responsibility: Assuming the Court grants a two-level reduction for acceptance of responsibility under USSG §3E1.1(a), the United States agrees for purposes of USSG §3E1.1(b) that defendant timely notified authorities of defendant's intention to enter a guilty plea, and a three-level reduction would be appropriate under USSG §3E1.1.

Total Offense Level: Although the above calculation results in a total offense level of 44, because it is in excess of 43, the total offense level should be treated as a level 43.

With a Total Offense Level of 43, and a Criminal History Category of I, defendant's sentence under the advisory United States Sentencing Guidelines becomes life imprisonment. (See PSR ¶ 106). Pursuant to USSG §5G1.2(d), the sentences for each count of conviction should be ordered to be served consecutive to one another to the extent required to achieve the total punishment called for under the guidelines. In

this case, this means the advisory guidelines sentence is equal to the statutory maximum sentence of 50 years imprisonment. (See PSR ¶ 106).

The government intends to respond at sentencing to any request by defendant for a downward variance or departure from the advisory guidelines sentence of 50 years' imprisonment.

V. RESTITUTION

Pursuant to 18 U.S.C. § 3663A, restitution in this case is mandatory. Defendant has agreed to pay full restitution to all victims of the offenses, including relevant conduct victims. (PSR ¶ 4).⁵

The government agrees with the U.S. Probation Office that the total amount of restitution should equal the amount of actual loss, with defendant receiving credit for certain amounts recovered by the victims in this case. (See PSR ¶ 119). The presentence report calculates the amount of loss and, thus, the total amount of restitution, as \$215,530,041.39. (PSR ¶ 44).⁶

With the help of the Trustee of the Estate of Peregrine Financial Group, Inc., Case No. 12-27488, pending in the United States Bankruptcy Court for the Northern District of Illinois (Trustee), the government is in the process of preparing a list of all victims for inclusion as a sealed attachment (attachment A) to the Judgment in this matter. The list will include all victims with PFG commodities futures accounts

⁵ At sentencing, the government will argue that a portion of the restitution judgment is due and payable immediately. The government will request that any restitution judgment imposed is collectable by all available and reasonable means pursuant to 18 U.S.C. § 3664(m).

⁶ As noted above, SA Irwin's calculation, using the figures as of the close of business on July 6, 2012, results in a total loss of \$215,530,547. (Gov. Ex. 9).

(excluding house accounts and related-entity accounts) with positive balances as of July 9, 2012.

The government anticipates the list of victim accounts⁷ in this case will exceed 10,000 names – presenting unique challenges with regard to distribution and accounting. Indeed, under normal circumstances, the Court may well determine that “the number of identifiable victims is so large as to make restitution impracticable” for purposes of 18 U.S.C. § 3663A(c)(3)(A) and dispense with an Order of restitution pursuant to 18 U.S.C. § 3663A(c)(3).⁸ However, at the government’s request, the Trustee has agreed to receive and distribute any restitution payments consistent with his duties as Trustee.

Accordingly, the government (with approval of the Trustee) proposes the following language for the Court’s restitution Order:

Restitution in the amount of \$ _____ is ordered to be paid, pro rata, to the victims listed in attachment A. The clerk shall forward any restitution payments to the Trustee of the Estate of Peregrine Financial Group, Inc., Case No. 12-27488, pending in the United States Bankruptcy Court for the Northern District of Illinois, for distribution to the victims in accordance with this judgment and sentence and the United States Bankruptcy Code. Any restitution payments received after the Trustee has filed his Final Report and the bankruptcy case of Peregrine Financial Group, Inc. has been closed will be disbursed by the clerk of court in accordance with this judgment and sentence.

⁷ In accordance with PFG’s system of records, some accounts are identified by a designation other than the victim account-holder’s name. The government submits that using PFG’s manner of designation on attachment A will best facilitate the distribution of restitution payments.

⁸ This is particularly so given defendant’s agreement to forfeit a money judgment in the amount of \$100,000,000 (and in view of the remission process established under 21 U.S.C. § 853(i) and 28 C.F.R. Part 9), as well as the early involvement of the Trustee and a court-appointed receiver who have been gathering PFG’s and defendant’s known assets for distribution to creditors including the PFG commodities futures account holders. Indeed, it may well be that only relatively small amounts of money will be collected as part of the restitution process, and that an independent distribution process would prove unworkable given the large number of victims.

Once the Trustee has submitted his final report, the government intends to use the Trustee's final accounting to determine how any future restitution payments should be disbursed.

The government asks that the Court order restitution accordingly.

VI. CONCLUSION

For the above reasons, the government asks that defendant's objections to PSR be overruled, that the Court order restitution in accordance with the above, and that the Court sentence defendant consistent with any additional record made at sentencing.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that I electronically served a copy of the foregoing document to which this certificate is attached to the parties or attorneys of record, shown below, on January 22, 2013.

UNITED STATES ATTORNEY

BY: s/ S. Van Weelden

COPIES TO: Jane Kelly